THE FREEMAN

IDEAS ON LIBERTY

How to Stop Wars

A Bad Time for Giants

Disasters Unlimited

Cyclical Unemployment

APRIL 1986

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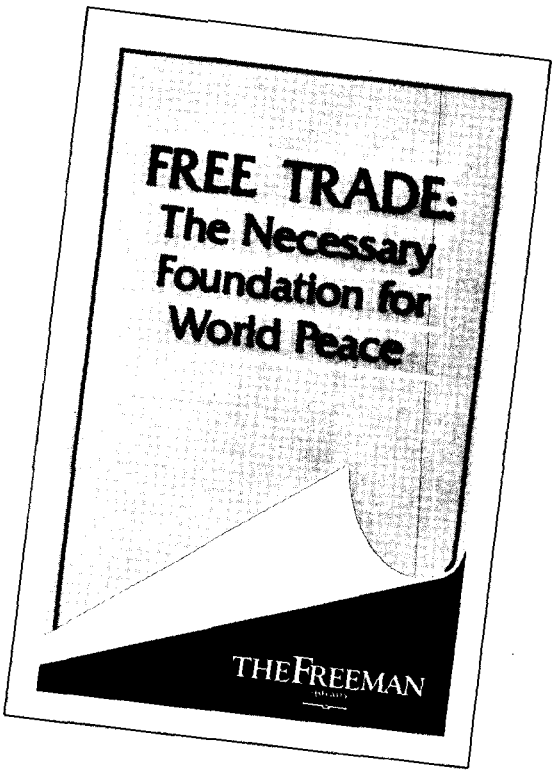
Introducing the first volume from *The Fre...*

Free Trade:
The Necessary Foundation for World Peace

edited by Joan Kennedy Taylor



At a time when public attention is turning to import quotas and other protectionist measures, many voices are being raised in support of the economics of free trade. But there is a deeper, often neglected truth—free trade can help ensure our survival as well as our prosperity. Protectionism can be seen by other nations as an act of hostility that in itself makes international conflict more likely. Free trade, by contrast, deepens the social bonds among those same nations and makes it in their self-interest to seek the peaceful resolution of conflicts.

To place free trade in this larger context of foreign relations, we have mined the back issues of *The Freeman* and other hard-to-find primary sources. Here are fifteen short essays that discuss such thorny issues as world hunger, industrial superiority, industrial unemployment, the American Revolution, foreign investment, the fallacies of economic nationalism, and how free trade protects our national interests. The thirteen authors represented are William L. Baker, Frederic Bastiat, Clarence B. Carson, Frank Chodorov, W.M. Curtiss, Bettina Bien Greaves, Henry Hazlitt, Samuel H. Husbands, Ludwig von Mises, Gary North, David Osterfeld, E.C. Pasour Jr., and Hans Sennholz.

This is the first volume in **The Freeman Library**, a new series of books that will, from time to time, bring together in permanent form a group of essays that illuminate a single topic. The Introduction for **Free Trade: The Necessary Foundation for World Peace** is by *The Freeman's* publisher, Paul L. Poirot.

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The Decline of OPEC

The recent collapse in crude oil prices seems to have taken OPEC by surprise. Perhaps they would have been better prepared had they read University of Virginia Professor S. Fred Singer's 1984 anthology, *Free Market Energy*. Addressing the question of "Future Oil Demand," Singer wrote:

"Saudi Arabia and the other 'core' producers made two principal mistakes: (1) in 1979–80 they permitted the price of oil to rise; and (2) they did not bring it down right away . . . The Saudis apparently misjudged the degree of conservation the price rise would precipitate among consumer countries. . . .

"When consumers expect prices to rise, they will install insulation and other heat-saving devices or buy more fuel-efficient cars. Once the investments have been made, they are not likely to be reversed, even if oil prices go down. Industry has been particularly effective in making such changes, introducing new and efficient processes and replacing old machinery with energy-saving equipment, with particular emphasis on substituting other fuels for oil."

Consumer sovereignty, more than any other factor, has reduced world oil prices to current levels.

Borrowed Time

The national debt recently topped $2 trillion, and is climbing ever higher.

What does this mean for the average American? According to a recent study by the Tax Foundation, for every man, woman, and child in the United States, the Federal debt will reach $8,600 by the end of 1986, an increase of nearly $900 in a single year. This figure has quadrupled in little more than ten years.

What is the cause of this burgeoning debt? The study concludes:

"The debt grows because the American people are receiving government benefits, but passing on the costs of these goodies to future generations. More importantly, the debt is growing because interest charges on the debt are growing and the principal is not being repaid. In other words, more and more of the debt is caused by debt. And the process seems locked in an inescapable spiral."

Thirty Years Ago

In the April 1956 *Freeman*, Leonard E. Read, founder and president of The Foundation for Economic Education, contributed his insightful essay, "On That Day Began Lies." He started by quoting one of his favorite authors, Leo Tolstoy:

"From the day when the first members of councils placed exterior authority higher than interior, that is to say, recognized the decisions of men united in councils as more important and more sacred than reason and conscience; on that day began the lies that caused the loss of millions of human beings and which continue their unhappy work to the present day."

These are powerful words, evoking images of Star Chambers, pogroms, and concentration camps. We Americans are inclined to feel safely removed from such proceedings. But coercion is often subtle, and when we act in a group, it is sometimes difficult

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to see the full import of our actions. Read brought the issue home with a parable he was to use in hundreds of FEE seminars:

Imagine this: Joe Doakes passed away and floated up to the Pearly Gates. He pounded on the Gates and St. Peter appeared.

"Who are you, may I ask?"

"My name is Joe Doakes, sir. I plead admittance."

St. Peter scanned his scroll and said, "Yes, Joe, you are on my list. Sorry I can't let you in. You stole money from others, including widows and orphans."

"Mr. St. Peter, I had the reputation of being an honest man. What do you mean, I stole from widows and orphans?"

"Joe, you were a member, a financial supporter, and once on the Board of Directors of the Updale Do-Good Association. It advocated a municipal golf course in Updale which took money from widows and orphans in order to benefit you and a hundred other golfers."

"Mr. St. Peter, that was The Updale Do-Good Association that took that action, not your humble applicant, Joe Doakes."

St. Peter scanned his scroll again, slowly raised his head, and said somewhat sadly, "Joe, The Updale Do-Good Association is not on my list, nor any foundation, nor any chamber of commerce, nor any trade association, nor any labor union, nor any P.T.A., nor any church. All I have listed here are persons, *just persons.*"

How to stop the collectivized lies which threaten people everywhere? Read concluded:

"It is simply a matter of personal determination and a resolve to act and speak in strict accordance with one's inner, personal dictate of what is right—and for each of us to see to it that no other man or set of men is given permission to represent us otherwise." □

Publisher: Paul L. Poirot
Senior Editors: Beth A. Hoffman
Brian Summers

Book Review Editor: Edmund A. Opitz
Contributing Editors: Robert G. Anderson
Howard Baetjer Jr.
Bettina Bien Greaves
Gregory F. Rehmke
Joan Kennedy Taylor

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THE FREEMAN
IDEAS ON LIBERTY

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How to Stop Wars

When trade is truly free, peace is present.

by Dean Russell

Dr. Russell teaches economics and is the author of *Government and Legal Plunder*, published by FEE.

For thousands of years, nations have fought each other to get "raw materials," which they then usually refused to share with other nations. Thus the wars go on, from one generation to the next—almost always to get goods and services that would have been readily available at lower prices (in blood, as well as money) if markets were free.

More than anything else, that's what free trade is all about—peace. For when trade is free (truly free, in all nations, among all people), peace is necessarily present. It is the only possible arrangement to accommodate that peaceful activity. But when trade is forbidden, a form of war automatically exists to some degree—both within nations and among nations.

Some unknown writer a hundred years or so ago expressed that sentiment on free trade and peace in dramatic terminology: *If goods don't cross borders, armies will.* He was right.

If I could travel freely in Russia, and trade my goods and services with like-minded Russians on terms negotiated by us as traders, it would be impossible to induce me to spoil that desirable arrangement by fighting them. It works both ways. What in the world would we fight about if we could peacefully visit and trade with each other; baseball versus ballet?

But as it is, I am literally scared of the Russians. I just don't know what they're doing behind those walls that are designed to keep their own people in and me out. Perhaps they're plotting against me. Maybe they even want to kill me. Since I don't know for sure, perhaps we'd better send more missiles to Europe. Be prepared, whatever the cost. I just don't trust people I can't visit and trade with.

When you get right down to it, that's the basis of fear, as well as wars that grow out of fear, i.e., it's mostly lack of information. And I'm quite sure it works both ways. The Russians are doubtless as scared of me as I am of them. That "fear of the unknown" will begin to evaporate when individuals and groups from one country have full

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If goods don't cross borders, armies will.

opportunity to travel and trade freely in other countries. *That's* the secret of peace; and in its absence, the best we can hope for is an armed-to-the-teeth standoff.

While I'm quite certain that the path to peace is the abolition of all restrictions on trade and travel for peaceful persons in any nation, I don't know how to persuade the Russians to agree. Their system of common ownership of all means of production and distribution seems to forbid much (if any) trade between individual Russians and individuals from other countries. For how can you trade with a person who can't own resources of any kind?

Even so, before we begin to fret unduly about the part to be played by the Russians in this vital process toward world peace, a prior step is needed. We've first got to agree among ourselves here at home that a free market for all goods and services among peaceful people is preferable to the controls we now have. I suspect that task will keep us busy for a few years yet to come. □

No Restrictions

IDEAS ON LIBERTY

FREE TRADE, as I would define it, can only exist when there are no restrictions on either side. Therefore, it is absurd to think of its existing in the world today with practically all countries operating under some degree of socialism. But, I would argue that it is to our own advantage to remove *our* restrictions, then trade as best we can under the restrictions imposed by other nations. It would be far from ideal, but their restrictions are basically their responsibility and not ours. My entire argument is based on what I think would be best for our own citizens, as producers and consumers, and I am not too much concerned with policies of other nations, however foolish I may think they are. Perhaps I should say I am concerned, but it is not within my province to try to force their reform. . . .

I believe that the principle most commonly lost sight of in our discussions of trade is that consumption is the sole purpose of production. We sometimes tend to think that the preservation of an industry or a particular firm or a man's job is the important thing to preserve. This leads to all sorts of uneconomic measures which adversely affect the consumer—the king.

W. M. CURTISS,
"Removing Our Trade Barriers"

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A Bad Time for Giants

Big can be beautiful, if we let the market and consumer demands decide.

by John K. Williams

The Reverend Dr. John K. Williams has been a teacher and is a free-lance writer and lecturer based in North Melbourne, Australia.

Samuel Goldwyn once remarked that he would like to make a film "which begins with an earthquake and works up to a climax." In so speaking, the film mogul gave voice to the spirit of an age which positively valued the big, the spectacular, and the colossal, an age in which the slogan, "The bigger, the better!" accurately expressed a widely held attitude.

Today, popular sentiment has undergone a change. The world, by and large, looks with suspicious eyes at bigness. Large nations, large cities, and large corporations are portrayed as sources of mischief. General Motors can do nothing right. The college president planning expansion is an "empire builder." A squatter holding out in an abandoned tenement building against developers is an heroic David taking on a gargantuan Goliath. "Small," we are informed, "is beautiful," and the converse of that somewhat breathtaking generalization is that "Big is ugly." It is a bad time for giants.

Critics of market capitalism in a classically liberal social order are conspicuous among those who equate "bigness" and "badness." Market capitalism, it is claimed, has undergone a mutation. Once upon a time it may have been true that the market curbed the activities of businessmen and industrialists, but no more. Market capitalism has given way to "late capitalism" or "monopoly capitalism." Giant corporations have rid themselves of the constraints imposed by Lilliputian consumers, and today stride the world. They manipulate the masses and treat governments as playthings. The big, the bad, and the ugly rule.

It is easy, and legitimate, to dismiss *socialists* who so characterize market capitalism. Whatever else market capitalism in a liberal society may be or do, it maintains institutions relatively free from the organisms of the state, the most massive concentration of power in human history. Socialists, in advocating an economic system coordinated by political edicts as against market forces, are advocating rule by a giant to end all giants: an all-present, all-powerful, and allegedly all-knowing giant. For such people to deplore the large institutions characterizing modern capitalist nations is, surely, the height of inconsistency.

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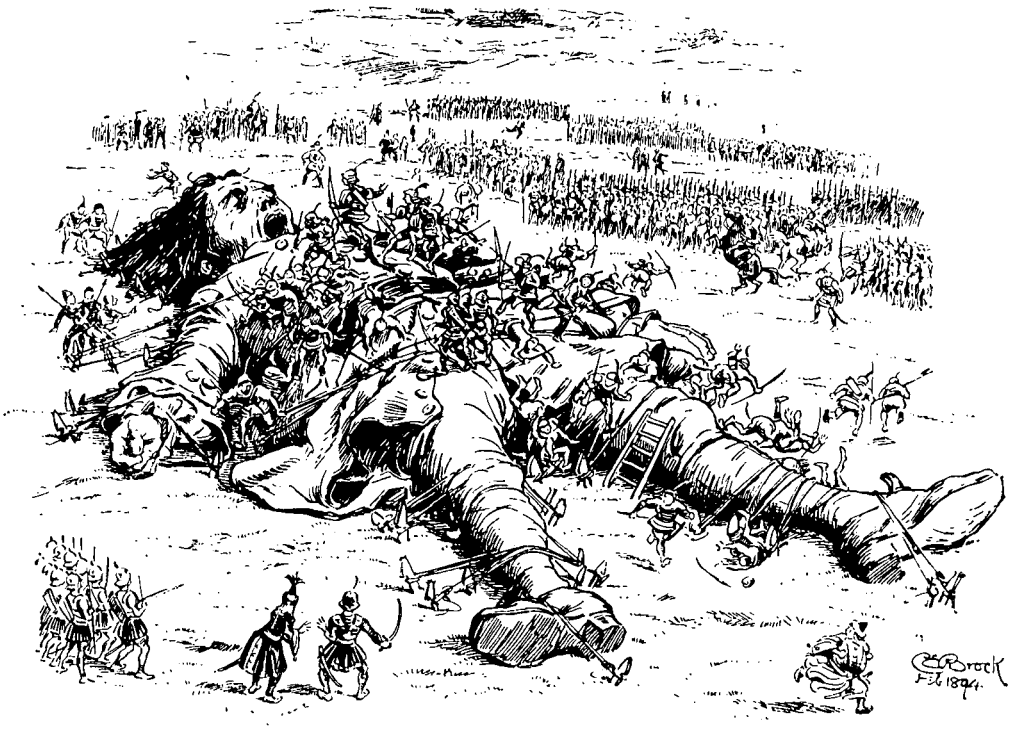

BETTMANN ARCHIVE

Yet, not all people who assert that market capitalism has undergone a metamorphosis advocate a socialist alternative. The claim that market capitalism in a liberal society is inherently unstable merits thoughtful examination, whether or not that claim is accompanied by the prescription of an alternative socio-economic system.

How Big Is "Too Big"?

The simplest version of the claim that market capitalism generates excessively large and unconscionably powerful corporations is grounded *not* in any economic or social theory, but in ordinary perception. An Australian church paper recently editorialized thus: "Giant corporations move in a world ordinary people do not understand. The balance sheets of these corporations casually refer to projects involving hundreds of millions of dollars. Corporate structures are complex and impersonal. What can these corporations know of the needs and frustrations of the average person? How can such a person, dwarfed by massive conglomerates, sensibly be described as free?"

Clearly, these rhetorical questions can be taken seriously and answered. Yet so to do in a sense misses the point. An attitude is being expressed rather than an argument being developed. The attitude is composed of suspicion, of resentment, and even of fear.

The words "big" and "small" are *relational* terms. A "big" dog is simply a dog larger than most dogs; a "small" house is simply a house smaller than most houses. Hence, when someone asserts that a corporation is "too big," the question, "Big in relation to what?" must be asked. Simply, the claim that a corporation is "too big" in the sense that the corporation is big in relation to a solitary individual, is little more than an expression of the sort of disquiet some people experience when observing the vastness of the Grand Canyon. The claim, as noted, is understandable. Nonetheless, it is irrational.

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Perfect Competition

In sharp contrast to this nonrational, almost phobic suspicion of the large corporation, a highly abstract and intellectual framework can function as a context for antagonism to such a corporation. This framework, elaborated in most standard economic textbooks, is the theoretical model described as the "perfectly competitive" or "purely competitive" market.

The world depicted in this model is far removed from what observedly is the case in developed, capitalist nations. In this theoretical world, no firm's activities have any appreciable effect upon the market, nor does any firm so satisfy consumers that entry into the market might prove difficult for people planning to produce and trade the same good or service. My ten-year-old nephew, Patrick, who breeds parakeets in a small aviary at the bottom of his parents' garden and sells these, is probably a producer of sorts whose activities satisfy these criteria. The activities of General Motors or of I.B.M. would not.

Again, the parakeets bred and sold by my nephew are, despite his protestations to the contrary, very much like any other parakeet, and thus comply with a further criterion for perfect competition: the product traded must be *homogeneous*, indistinguishable from that traded by any firm manufacturing the same sort of good or providing the same sort of service. As noted, even my nephew insists that his parakeets are, by virtue of the secret mixture of seed he feeds them and the love he gives them, "better" than other parakeets sold in the market. Certainly, most firms in the real world diligently strive to produce goods differentiated from those of their fellow producers.

Most startlingly, participants in a perfectly competitive market are quite unlike the fallible, fumbling, finite beings one encounters in the real world; sellers and buyers alike possess, in the world of perfect competition, perfect knowledge and unerring foresight. Confronted by a vast array of possible choices, all of which are somehow known to them, they infallibly and instantaneously select the optimum option. No unwanted situations arising out of human ignorance or errors of judgment exist.

This abstract, theoretical model has very limited applicability in the real world. The absence of a plethora of tiny firms manufacturing or providing an absolutely homogeneous product or service is in no sense ominous. *No static model depicting an ideal allocative outcome of market processes captures the essence of a capitalist economy.* Joseph Schumpeter puts it well: "Capitalism . . . is by nature a form or method of economic *change* and not only never is but never can be stationary." Indeed, Schumpeter is worth quoting at length. "In capitalist reality as distinguished from its textbook picture, . . . [the] kind of competition which counts . . . [is] competition from the new commodity, the new technology, the new source of supply, the new type of organization." This form of competition "acts not only when in being but also when it is merely an ever-present threat. *It disciplines before it attacks.*"

The abstract model of a perfectly competitive market depicts a situation in which all potential mutually beneficial transactions have been realized. A state of equilibrium obtains. In the real world of changing circumstances and human finitude, *disequilibrium* is the reality. The *absence* of equilibrium generates in a market economy systematic entrepreneurial activity that tends to eliminate existing imbalances, mov-

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"Market capitalism can only be understood in terms of ongoing market processes, not any particular static allocative outcome of these processes."

ing the situation closer to an hypothesized state of equilibrium defined by the market data which obtained prior to the beginning of this entrepreneurial activity. Yet before this activity results in even an approximation to this hypothesized equilibrium state, the data of the market will have changed. People's tastes will have altered; available resources will be marked by different relative scarcities; new technologies will have been born; new ideas will have emerged. A new state of disequilibrium exists. Further entrepreneurial activity is thus generated. On and on the process goes. *Market capitalism can, in other words, only be understood in terms of ongoing market processes, not any particular static allocative outcome of these processes.*

Non-Market Decision Making

Had one asked a typical mainstream economist some two decades ago to outline a desirable program of governmental economic management, he or she probably would have insisted upon fiscal and monetary policies to promote macroeconomic stability. Some sort of antitrust legislation, regulation, or nationalization of natural monopolies would be proffered. Subsidization of various activities productive of positive externalities (especially education and research), and taxation policies promoting greater economic equality, would also be eagerly promoted.

More recently, however, mainstream economists have seriously questioned the theories of so-called "market failure" and of governmental behaviors informing such a program. It is conceded that such abstract and simplified models as the perfectly competitive market assume away institutional details which may in fact fulfill an extremely useful purpose. More significantly, it has become clear that while governments eagerly embrace rationalizations for intervention in the market—and that many economists are no less eager to elaborate such rationalizations—governments have their own purposes. The dynamics of political processes are such that the outcomes of intervention may be quite other than those intended by economists. Similarly, bureaucracies have built-in incentive structures which largely determine the way they perform. Some disillusioning observations have led to a heightened interest in comparative institutional analysis, in which deterministic theories of the performance of market, government, and bureaucratic institutions are deduced from their underlying incentive structures, on the assumption that decisionmakers are rational and desirous of improving their own situations.

Insights provided by this sort of analysis confirm what Ludwig von Mises long ago asserted, namely, that non-market decision-making entities have serious deficiencies with respect to the weighing or registering of individual preferences, the taking of a long-term point of view, operating at a low cost, and, generally, achieving an allocation of resources closer to that suggested by an ideal of perfect coordination

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than does an unfettered market. In short, *many mainstream economists working within the framework of perfect competition now argue that intervention is warranted only when they allegedly totally default, not when they allegedly marginally default.*

The notion of perfect competition does, in emphasizing ease of entry into and exit from the market, serve as a reminder that *any alliance between government and any set of market participants, union or business, is anathema, jeopardizing freedom of market entry.* The maximum wage laws that cursed the political economy called mercantilism, and the minimum wage laws cursing most Western nations today, are cases of such an alliance. So are tariffs, quotas, price-maintenance schemes, subsidies, laws dictating shopping hours, price controls, and the plethora of regulations today fettering most Western economies. That the market continues to operate when so bound and burdened is testimony to its hardiness. How long it can continue to operate when its nervous system—changing relative money prices—is subject to ever-increasing distortion, is not, however, clear.

One thing, however, *is* clear. Antagonism to large corporations based upon the disparity between the actual operation of market economies and the defining characteristics of perfectly competitive or perfectly contestable markets is misguided and misplaced.

"Late Capitalism"

During the late 1950s, Ludwig von Mises delivered a series of lectures on economic topics to Argentinean audiences, subsequently published as *Economic Policy.* He did what only a master of any academic discipline can do: simplify complex issues without distortion. He commenced his first lecture thus:

> Descriptive terms which people use are often quite misleading. In talking about modern captains of industry and leaders of big business, for instance, they call a man a "chocolate king" or a "cotton king" or an "automobile king." [Yet] . . . a chocolate king does not rule at all; he *serves.* He does not reign over conquered territory, independent of the market, independent of his customers. The chocolate king—or the steel king or the automobile king or any other king of modern industry—depends on the industry he operates and the customers he serves. This "king" must stay in the good graces of his subjects, the customers; he loses his "kingdom" as soon as he is no longer in a position to give his customers better service and provide it at lower cost than others with whom he must compete.

The vision is clear. Consumers, by their decisions to buy or abstain from buying, determine what is produced and in what quantities. Ultimately they determine the prices at which goods are sold, the choice of means whereby goods are produced, and the remuneration received by all participants in the productive process.

Such, say many contemporary critics of market capitalism, was once the ideal and perhaps once was the reality. But no more. Large corporations have dethroned the consumer. These critics range from socialist politician Michael Harrington to Marxist-Leninist economist Paul Sweezy. But perhaps John Kenneth Galbraith best reflects the general attitude.

Writes Galbraith: "So far from being the controlling power in the

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economy, markets [are] more and more accommodated to the needs and convenience of business corporations." Corporations are controlled not by consumers, but by the faceless, anonymous "experts" constituting what Galbraith calls the *technostructure,* people possessing the information and expertise necessary to design a product, to acquire capital, to modify people's taste, and so on. Informed by this technostructure, corporations exercise an unchallenged sovereignty. The giant has flexed his muscles, freed himself of all constraints, and thus today exercises unfettered power both nationally and internationally.

Galbraith's views, eloquently expressed, brilliantly advertised, and attractively packaged, have successfully been sold to many members of the general public, and to countless "fringe" academics and influential journalists. Most economists have manifested considerable sales resistance. Professor Harold Demsetz asserts, "The only conclusion permitted by [my] investigation is that Galbraith's notions are remarkably consistent in their inability to find confirmation . . . . Columbus had a great deal more corroboration for his belief that he found the Indies than Galbraith has for his discovery of the new industrial state." George J. Stigler and James Kindahl, in a major study commissioned by the National Bureau of Economic Research, conclude, after exhaustive investigation, that the claim that "prices of concentrated industries do not respond to reductions in demand" runs counter to all the evidence.

In sum, the economic attack on large corporations collapses. The desperate attempts to demonstrate that large corporations need no longer seek to serve consumers have failed and failed dismally. Indeed, as simple an exercise as the persual of the *Fortune* top 500 companies over a period of time suffices to raise a question mark against their simplistic, but widely accepted, assertions. Of the original 500, only 285 remained two decades later; 159 had merged, 50 had either gone bankrupt or shrunk, and 6 could not be classified, the data necessary for classification being unavailable. So much for the unchallengeable sovereignty of the modern corporation!

The Transnational

But what, it may be asked, about these malicious, monstrous corporations which feast at tables groaning under the bounty secured by global plunder: transnational corporations? Are they not, in the words of Richard Barnett and Ronald Miller, "disturbers of the peace on a global scale"? Did not the Sixth Assembly of the World Council of Churches, held during 1983 in Vancouver, declare its avowed opposition to transnational corporations, insisting that the world's "market system as a whole . . . [is] incompatible with our vision of a just, participatory and sustainable society" and rapturously applaud Jan Pronk, Deputy General Secretary of the United Nations Conference on Trade and Development, when he informed a plenary session of the Assembly that the New International Economic Order would bring to all people the advantages of "international democratic socialism"—albeit not explaining how that cabal of tyrannies could establish a democratic order of any kind whatsoever? Does not everybody *know* that transnational corporations today constitute "the spearhead of U.S. imperialism"?

Oddly, not everyone *does* know that. The Marxist-Leninist dictator

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of Zimbabwe, Robert Mugabe, apparently does not know how terrible transnational corporations are, for when visiting New York in August, 1980, he pleaded with the heads of transnational corporations to invest in Zimbabwe, stating, "Union Carbide has done much good for Zimbabwe. Why can't other companies as well?" John Kenneth Galbraith does not know how evil such corporations are: in an article published in 1978 in the *Harvard Business Review* he ridiculed the obloquy typifying most discussions about transnational corporations. (Such support, admittedly, is ominous: If Galbraith approves of transnational corporations there must, surely, be something suspect about them. The careful reader of Galbraith's article will observe, however, that Galbraith perceives in transnational corporations organizations large enough and powerful enough *totally* to bypass consumers and deal the *coup de grace* to whatever remains of consumer sovereignty. Since Galbraith deplores the tastes of the masses and dreams of a day when intellectuals sharing his values control socio-economic systems, the complete elimination of any vestiges of consumer sovereignty is to be desired. Galbraith fails dismally to demonstrate that transnational corporations can so defy the rule of consumers. He does demolish most of the fashionable objections to such corporations.)

Interestingly, some economists commissioned by the International Labor Office in 1975 to prepare a series of studies on transnational corporations, documented some embarrassing truths. They noted that such corporations had created two million jobs in developing nations, usually had replaced expatriate managers with host-country nationals as soon as was feasible, and scrupulously had respected the host country's social values and labor relations practices.

Indeed, transfers of wealth effected by transnational corporations have demonstrably been of more assistance to the people of developing nations than have most government to government transfers. Such private transfers are considerable. There is the transfer of capital involved in building factories and plants. There is a transfer of *human* capital, host country nationals acquiring new and valuable skills. Wages paid to employees can, given sensible taxation policies, lead to saving, capital accumulation, and the creation of local industries. Typically, when transnational corporations invest in a developing nation, schools and hospitals are erected and considerable funds are invested in infrastructure, such as roads and sewerage.

Some Telling Arguments

Strangely, some of the most telling arguments in favor of transnational corporations are unwittingly provided by their opponents. Richard Barnett notes that the power of such corporations is a function of their capacity to internationalize planning, financing, production, and marketing. Has he not heard of comparative advantage? Is it not *desirable* that the different strengths of different nations should be linked? Is not a world of interdependent nations a safer world, as well as a wealthier world, than a world of unrelated nations desperately struggling to achieve self-sufficiency? Again, the Brandt Commission laments the "ability of [transnationals] to manipulate financial flows by use of artificial transfer prices" and notes that such corporations "have been able to race ahead in global operations and out of reach of effective controls by nation-states or international organizations."

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Informing this condemnation of transnational corporations is a fiction: that the interests of rulers and the interests of the ruled invariably coincide. This is, admittedly, a useful fiction from the point of view of the rulers, but it is a fiction nonetheless. Governments busily inflating the money-supply of a nation are doubtlessly assisted in their task by stringent exchange controls. The economy of the nation—and hence the vast majority of the nation's people—does not benefit. Protectionism and the savage customs duties protectionism demand feed economic inefficiency and high prices. Do these realities benefit the people? Bluntly, *at long last governments, largely thanks to transnational corporations, are being forced to compete.* Such is cause for hope, not dismay.

Yet such hope is conditional. When governments and corporations form an unholy alliance and substitute an invisible handshake for the invisible hand of the market, mischief is afoot. Many corporations today bask in special privileges and actively enjoy an alliance with government. When such alliances exist, either in a developed or a developing nation, an obscenity has been spawned.

To suggest that an admittedly deplorable overlap between corporations and governments calls for the total subordination of a nation's economy to the state, is an obvious *non sequitur.* It also proposes as a remedy a more deadly variant of the disease from which Western nations today suffer. That remedy—and its name is socialism—has, after all, been tried. It has reduced once wealthy nations to destitution. It has transformed liberty into slavery. It has destroyed the only means a people possesses for so allocating scarce resources that food sufficient for all to eat is produced and the specter of poverty is exorcised.

Conclusion

"Small is beautiful." Sometimes it is. Sometimes, however, it is disastrous. Warm-blooded animals in a cold environment must be above a certain size or they will perish. That is why there are polar bears, but no polar mice.

The same can be said about organizations and the economic environment. The free market, and that presupposes a limited but strong government respecting the autonomy of each citizen and protecting the God-given liberties of all, alone can determine what size is the "right size" for any business or industry. So long as growth enables a corporation better to serve its customers, such growth is desirable and such growth will continue. When growth lessens a corporation's capacity to serve the people, a red light is flashing. That corporation must cut back, or its days are numbered. Sadly, but understandably, the temptation is for the corporation to plead with government to save it from the unpleasant alternative of painful change or destruction.

Consistent advocates of the free market in a free and open society must say "No!" to such pleas. Neither we nor anyone else can say in advance what size is the "right size" for a particular business enterprise. Yet we can say, and say with confidence, that the free working of the market will enable that "right size" to be discovered. Hence, when corporations and the State start coyly flirting, we do well to appoint ourselves to the "spoilsport" role of chaperones. A love affair almost guaranteed to produce mutant giants or dwarfs must, in all charity, be nipped in the bud! □

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Disasters Unlimited

When disaster subsidy zones are created, disasters proliferate and tragedies continue.

by John W. Sommer

Dr. Sommer is President of the Political Economy Research Institute in Dallas, Texas and is an Adjunct Scholar of the Cato Institute in Washington, D.C.

Almost one thousand years ago in England a subtle lesson in the limits of public authority was offered by King Canute who, when implored by fawning courtiers to demonstrate his regal powers by commanding the ocean waves to halt their assault of the shores, waded into the surf, held up his hand in mock gesture, and permitted all to observe his royal drenching. Canute could not avoid the force of Nature. Today, government intrusion into these areas produces a severe loss of individual responsibility and leads to the prospect of an all-powerful government attentive to special interests.

Public actions to forestall physical events or to provide relief antedate Canute of course, stretching back to Sumerian days. Fires, floods, droughts, earthquakes, hurricanes, tidal waves, tornados and volcanic eruptions lead a list of natural disasters which has been extended in modern times to include technological hazards such as toxic wastes, nuclear reactors and other remotely plausible threats. In fact, the list is infinitely expandable, perhaps one day to include denture stains and psychological damage from viewing old reruns of "The Honeymooners." Anything is possible when individuals become convinced that the shield of the State can, and rightfully should be deployed to protect their life and property at all times, in all places of their choosing, and under any circumstance.

This belief in the function of the State as the proper intervenor in all events of calamitous consequence is promoted by a triangle of special interests: 1) Citizens who are at risk or have just experienced a disaster try to reclaim some of their taxes in the form of payment for actual losses, or in the form of localized public investment such as dams or sea walls, to forestall future losses. 2) Politicians "recognize the wisdom of the people" and even exert leadership by "helping" constituents to recognize previously unforeseen threats. Congressional representatives thrive when they deliver public works thought to be hazard mitigating (and known to be vote generating). 3) Bureaucrats seek to expand the scope of their preparedness and the size of their budgets. Each party responds to the logic of incentives. This *beneficial triangle* is a benign system when viewed from the vantage of intent, but it has a tumorous quality in terms of consequences.

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The systematic consequences of the humane urge to protect or assist people, and to be protected and assisted, requires vigorous national attention to illuminate the reasons why voluntary disaster assistance is superior to public liability of current and future Americans who are placed in debt for the protection of their countrymen. Such attention may, at the least, help to stem the tide of disaster creation. The logic of the argument may help to return us to a society wherein market calculations replace the beneficial triangles and where voluntary relief organizations may flourish.

Disaster Subsidy Zones

In 1803 Congress gave the first disaster relief in the form of an extension of time for discharging customhouse bonds of sufferers from fire in Portsmouth, New Hampshire. It did the same for Norfolk, Virginia the next year. Over the intervening years Congress has increased the number and size of awards as well as increasing the kinds of disastrous events which qualify. From the first award in 1803 to 1953 one hundred and fifty disasters were declared—or one per year on average.[1] In 1953 Congress granted the President authority to declare disasters. Since then the Presidency has expanded its powers to intervene in both past and potential disasters to the degree that "acts of God" are recognized only after a declaration of disaster by the Chief Executive!

Of course, the number of disaster declarations, and the amount of the awards have risen dramatically since 1953, as may be seen in the table below:

Federal Disaster Declarations 1803–1982[1]

Period	Average Number of Awards Per Year	Average Dollar Amount of Award	Largest Award in Period and Year
1803–1952	1	Not calculable	$ 15,000,000 (1943)
1953–1962	14	$1,630,000	$100,400,000 (1954)
1963–1972	28	$5,100,000	$351,500,000 (1972)
1973–1982	40	$6,400,000	$190,000,000 (1979)

Presidential perspicacity has "permitted" more disasters to be officially recognized and, in current dollars, the average awards have jumped from a little more than one-and-one-half million per disaster during the decade 1953–1962 to about six-and-one-half million per disaster from 1973–1982.

Disaster relief is extended to individual states upon application by the state. The largest awards during each period were for hurricane related damage: Maine in 1954, Pennsylvania in 1972, and Alabama in 1979. Of the many disasters declared, the most expensive have resulted from hurricanes which have wrought havoc on the Atlantic and Gulf coasts. When the Federal awards to each state are summed after a traumatic event the outlay is staggering. Hurricane Agnes, for example, evoked nearly half a billion dollars in Federal relief in five states in 1972, the greatest part of which, as is the case with most hurricanes, was damage caused by flooding. In fiscal 1985, the federal government spent about one third of a billion dollars for direct disaster relief and insurance—and there are many additional indirect outlays,

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"Under a governmental system of public support, 'disasters' are unlimited."

not to mention those of state and local government. Federal flood insurance, for instance, is subsidized to the extent that it costs those who qualify, by virtue of owning property in an official hazard zone and enlisting in the program, only about one-third of what private insurance premiums would be.

What we witness then is a cycle of destruction by traumatic natural events followed by a period of reconstruction underwritten by the public treasury. At the time of tragedy it appears inhumane to us as individuals to cavil over assistance to those stricken, and most Americans would choose to provide assistance to the injured and homeless. But we should expect the prudent use of that assistance, not rebuilding on the same hazard-prone sites under the protection of continued artificially low-risk premiums. That is exactly what happens with the use of public funds. *Disaster subsidy zones* are thereby created. The obvious result is that real estate investors build where otherwise they would not because the risk inherent in their locational choice is spread to all the taxpayers. This is as true of lowland riverine areas as it is of barrier islands and adjacent coastal areas. Is it a proper function of government to subsidize these individual choices?

Disasters Unlimited

It is in this sense of induced or subsidized settlement in these disaster-prone zones that the Federal government uses our tax monies to place individuals at risk. This seems to be unethical, as well as inefficient in an economic sense. By using the general treasury to guarantee reduced financial loss due to natural disasters, government makes known hazardous locations more inviting. Furthermore, it points to the inequity inherent in subsidizing the risks of some individuals while not recognizing those of others. Disaster subsidies are often a redistribution of income from the less wealthy to those who can afford coastal resort condominiums and homes with hillside vistas.

The vulnerability of these disaster subsidy zones is well documented. In 1900 Galveston was struck by a hurricane that killed 5,000 people. In 1983, Hurricane Alicia caused nearly $700 million damage to Galveston and nearby areas. Today, with extensive Federal relief, the devastated areas have been rebuilt and condominium developers are advertising views of the Gulf unblocked by sea walls! This history is repeated along our coasts.

Tornadoes, earthquakes and volcanic eruptions are also dramatic and costly, but they occur with less regularity to the same site. Despite the drama of these occurrences, after flood damage the next most costly natural event is shifting or expanding soil.[2] Boring! No television covering of this natural disaster! Soil movement cracks foundations and walls without raising any passion or pity, yet those who live in these soil-moving areas and suffer losses might wonder why they should subsidize ocean-view condominium owners while their own

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Why the President Said No

I return without my approval House bill No. 10203, entitled "An act to enable the Commissioner of Agriculture to make a special distribution of seeds in the drought-stricken counties of Texas, and making an appropriation [of $10,000] therefor."

It is represented that a long-continued and extensive drought has existed in certain portions of the State of Texas, resulting in a failure of crops and consequent distress and destitution.

Though there has been some difference in statements concerning the extent of the people's needs in the localities thus affected, there seems to be no doubt that there has existed a condition calling for relief; and I am willing to believe that, notwithstanding the aid already furnished, a donation of seed grain to the farmers located in this region, to enable them to put in new crops, would serve to avert a continuance or return of an unfortunate blight.

And yet I feel obliged to withhold my approval of the plan, as proposed by this bill, to indulge a benevolent and charitable sentiment through the appropriation of public funds for that purpose.

I can find no warrant for such an appropriation in the Constitution, and I do not believe that the power and duty of the General Government ought to be extended to the relief of individual suffering which is in no manner properly related to the public service or benefit. A prevalent tendency to disregard the limited mission of this power and duty should, I think, be steadily resisted, to the end that the lesson should be constantly enforced that **though the people support the Government the Government should not support the people.** [Emphasis added.]

The friendliness and charity of our countrymen can always be relied upon to relieve their fellow-citizens in misfortune. This has been repeatedly and quite lately demonstrated. Federal aid in such cases encourages the expectation of paternal care on the part of the Government and weakens the sturdiness of our national character, while it prevents the indulgence among our people of that kindly sentiment and conduct which strengthens the bonds of a common brotherhood.

— Grover Cleveland,
February 16, 1887

"disaster" goes unrecognized. Why should their locational choice be regarded as qualitatively less worthy of protection than the choices of others?

It is only a small step to recognize that any instance of change that is inconvenient is a risk and has potential to damage, therefore to be regarded a "disaster." Once providing disaster subsidies is accepted as a proper function of government, it is intellectually unassailable to expand the list of disasters to include such non-physical misfortunes as "damages" to border firms affected by devaluation of the Mexican peso, or to states impacted by Cuban refugee settlement. It is also attractive to the citizens, politicians, and disaster-bureaucrats who

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form the beneficial triangles identified earlier. Under a governmental system of public support, "disasters" *are* unlimited.

Government cannot shield each of us from any unforeseen event no matter how much personal freedom of action and decision is relinquished to the State. Yet there are those who argue that disaster preparedness is a public good. On what basis then should individuals turn over to the State the authority to decide whose exposure to change shall be mitigated and whose shall not? There are sufficient off-setting public bads resulting from this process, as indicated throughout this article, to demand curtailment of these incentives before more beneficial triangles come into being.

Backout Strategies

Risk and change are part of the human condition; everyone seeks to reduce the former and to direct the latter. How this is achieved is an issue of moral philosophy as well as political economy. Clearly, maximum individual choice in location decisions, subject to complete responsibility for one's actions, is superior in terms of ethicality and efficiency to our present system of hazard subsidy. The market in private insurance informs one of the likely consequence of choice of place and deals efficiently with risk without its subsidy. Equally clear, in the presence of resources held in common and territorial-based political representation, market signals are garbled. We know that we live in a contentious political economy, not a flexible market economy, and there are many in this country who profit by beneficial triangles which seek to mitigate the effects of change by distributing the associated costs to the public at large. Special interest abuses are expected when government is expansive, so it is no surprise that disaster subsidies have increased in the second half of the twentieth century.

We must forestall the development of new disaster subsidy zones and design *backout strategies* from those that exist. Gradually, we can move the system toward less costly and less threatening levels by adopting "sunset laws" which announce firm termination dates for the removal of disaster subsidies. These may be subject to a steadily reducing schedule of possible payments or a variety of other stipulations, but the central feature is the certainty of the removal of public support. We can also declare that no geographical location shall be eligible for Federal disaster relief for the same kind of disaster more than once. The field is open for creative backout strategies.

In the final analysis it is the responsibility of individuals to exercise judgment in action. Acceptance of this proposition will lead to private institutions to forestall disastrous events, or to mitigate their effects. Clearly, there is much latitude for individuals to engage in collective action to help their fellows when they are stricken. Private organizations do exist, and because their appeal is to conscience, not to Congress, one can expect a wiser deployment of resources. At least, in a private arrangement we can expect to avoid a systematic increase in disasters. □

1. United States of America. *Congressional Record.* Volume 96, Part 9, August 7, 1950, Washington, DC. U.S. Government Printing Office, 1950, pp. 11900-11902; *Ibid.* 4/30/73, pp. H3166-H3170; *Ibid.* 9/5/73, pp. S15951-S15952; and Federal Emergency Management Agency. DMIS Report 2.4. "Disasters Declared Under Public Law 93-288, April 1, 1974 to July 19, 1985."

2. D. Earl Jones, Jr., and Wesley G. Holtz, "Expansive Soils—The Hidden Disaster," *Civil Engineering* (August, 1973), p. 49.

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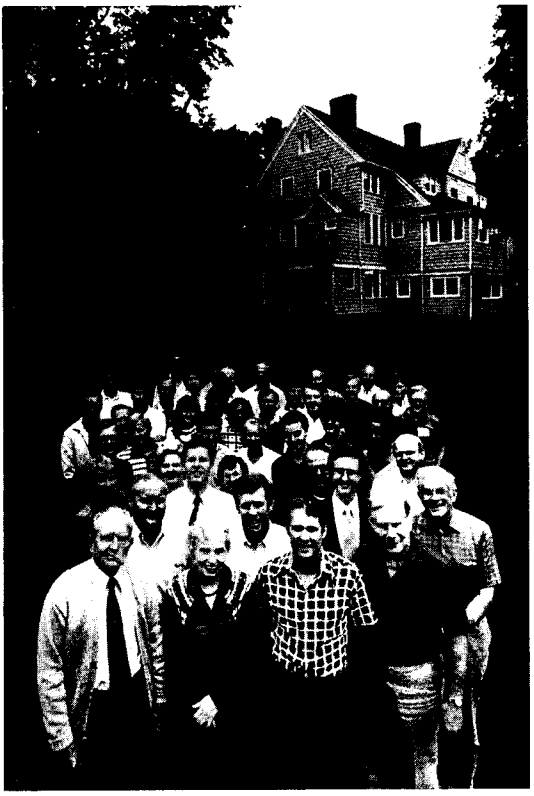

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The Right To Stagnate

When force is used to maintain the status quo, basic rights are violated.

by Frank W. Bubb

Frank W. Bubb is an attorney residing in Swarthmore, Pennsylvania.

Every society operates explicitly or implicitly on some theory of rights, that is, a generally shared view of who can do what to whom under what circumstances.

Most of us still pay lip service to the traditional American theory that each person has the right to "life, liberty and the pursuit of happiness" and to the free-market economics implied by that theory—with some important qualifications. Now, however, the qualifications have become so pervasive in practice that we have backed into an entirely different theory of rights.

The new theory could be described as follows: "The members of each major group in our society have the right to be maintained at the standard of living they have come to expect. If economic change threatens this standard, it is the duty of government to help the affected group."

For example:

- Thousands of American farmers have been facing financial ruin as their debt escalates while commodity prices remain low. Predictably, they appealed to the government for emergency low-interest loans. What is their justification? That they, the businessmen who borrowed to bid up prices of farmland in the boom years of the late 1970s, have the right to be made whole at the expense of the taxpayers, so they can live as if the boom had continued.
- American steelmakers have repeatedly brought proceedings before the U.S. International Trade Commission to prevent Americans from buying more than a certain percentage of their steel from abroad. How is the import percentage arrived at? To give U.S. steelmakers enough sales to remain profitable, so they can continue to operate as if they were the first choice of customers who would now rather buy elsewhere.
- In the annual battle over budget cuts, many politicians refuse to eliminate programs, instead favoring an across the board freeze so the pain is "shared equally." Why? Because every interest group that once mustered enough political power to obtain

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a subsidy is deemed entitled to that subsidy forevermore, regardless of its current merit.

- And what about those cost of living allowances on Social Security and government pensions? The purpose of a cost of living allowance is to make recipients whole after inflation. But inflation is a hidden tax, a way for the government to take additional resources out of the private economy. If some are allowed to live under the illusion that inflation is not a burden, then the burden on others is increased.
- My favorite example of our new theory of rights is tobacco farmers. Here is a group of people whose particular product is, in effect, a poison. Yet at the same time the federal government spends billions to counter tobacco's harm, it continues to subsidize tobacco farmers, apparently on the theory that it is "not their fault" that their product has been found dangerous.

We have traded "the right to life, liberty and the pursuit of happiness" for "the right to stagnate."

In these cases and countless others, politically cohesive groups use the power of government—the power to tax, the power to stop imports at the border, and so on—to shift the burden of coping with economic change to the unorganized mass of taxpayers and consumers.

The right to stagnate is nice, for those who have it. Unfortunately, it is not available to everyone. Since "change is the only constant," people must constantly adapt to it, whether they live alone or in groups.

A person who proclaimed his right to stagnate while living alone on a desert island would find his error quickly corrected by reality. In society, some people can live under the illusion that change can be stopped as long as they can find victims to bear its less desirable consequences.

The right to stagnate must be rationed, and the ration card is political power. Those groups which can organize most easily and whose members have the most to gain from government favors can always outmaneuver larger, less organized groups whose members have relatively little to gain or lose on any particular issue.

In *The Rise and Decline of Nations*, economist Mancur Olson details the correlation between economic stagnation and the power of special interest groups. Those societies which enjoyed long periods of stability—India and China through the ages, and in the last half-century Great Britain—have been choked by the accretion of interest group power. But those societies whose interest groups have been destroyed by war or revolution, such as Japan, Korea, and West Germany, or whose interest groups have been unable to keep pace with a rapid expansion of political borders, such as 19th-century America or the European Common Market in the 1950s, have had extraordinary economic growth.

Olson's analysis is basically pessimistic. Do we need war or revolution to unfasten the hold of special interest groups on the throat of our body politic?

Maybe, just maybe, a moral revolution might be enough. If enough people could recognize the right to stagnate for what it is, and start treating its proponents with the scorn they reserve for common thieves, we might yet realize the American Dream. □

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Cyclical Unemployment

In the final analysis, government is solely responsible for the business cycle and the unemployment that results.

by Hans F. Sennholz

Dr. Sennholz heads the Department of Economics at Grove City College in Pennsylvania. He is a noted writer and lecturer on economic, political, and monetary affairs. His most recent book is *Money and Freedom.*

Employment is an essential source of happiness and enjoyment. No man, properly occupied, can be miserable for long. To enjoy life, man must employ life, which ought to be his aim and aspiration. To be unemployed is to waste life and invite evil. And yet, millions of people who would like to be employed in the market for goods and services, are sporadically unemployed. They are the primary victims of business cycles.

Economic instability has been the lot of man since the beginning of time. Whether he made his living by hunting or fishing, by cultivating the land, or engaging in industry, commerce or finance, man always faced the vicissitudes of economic life. There were good times and bad times, but these changes were caused by such extraneous influences as crop failures, epidemics, civil strife, or war. Business cycles are modern phenomena—products of the modern economic order with its political conditions and institutions. The first business cycles in the modern sense were recorded in England during the second half of the eighteenth century. The first American depression is known to have taken place in 1819. In many parts of Europe, cycles did not appear until the middle of the nineteenth century, in Russia and Japan not until the end of the century.

Business cycles are visible changes that take place in business conditions over periods of time. Boom conditions are followed by spectacular crises and painful readjustments commonly called depressions. During the course of a cycle the factors of production are subjected to radical changes in demand; they may work overtime during the boom phase and be idle during the crisis. They may enjoy rising prices and incomes during the boom, and suffer staggering losses in the depression. Labor may reap rising wages and benefits during the boom and face unemployment during the depression.

Observers of the economic enigma readily offer their explanations. One group attributes the cycle chiefly to other than economic occurrences such as political incidents, to conflicts and wars, or to changes

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in the growth rate of population or international and intranational migration. Economists are quick to discard such "outside factors" because they are not inherent to the economic process.

Some economists attribute business cycles to accidental combinations of unfavorable economic circumstances. They are convinced that each depression has its own particular origins such as inadequacy in the stock of money, hoarding and scarcity of credit, over-investment in industry, new technology or real estate. "Practically every economic fluctuation," Joseph A. Schumpeter explained, "must be a historic individual and cannot be made amenable to explanation but by minute historical analysis of the innumerable factors actually at work in each case."[1]

Most students of the business cycle question the accidental-combinations theory. They are convinced that a single cause affects the economic system and generates the cyclical fluctuations. But they differ widely on the nature of the cause. The different explanations offered by distinct schools of thought may be classified according to the causative factors they emphasize:

I. The complexities of division of labor
II. The capitalistic system
III. Government intervention

The Complexities of Division of Labor

Many economists point at an "anarchy of production" resulting from the division of the production process as the cause of crises and the unemployment they engender. It is difficult, they assert, for businessmen with limited knowledge of the demand for their products to maintain equilibrium. Entrepreneurs and capitalists face great uncertainties that spring from the roundaboutness of time-consuming processes of production. Moreover, economic goods are produced to be exchanged, which invites errors of judgment that tend to develop cumulatively either toward optimism or pessimism.

A.C. Pigou, reflecting on the economic stagnation of the early 1920s, explained that two businessmen make "at the same time now an exaggerated, now an inadequate estimate of the other's prospective real demand for his stuff. No study of trade cycles can be adequate in which this point is misunderstood."[2] Professor Taussig, the foremost American economist of his time, pointed at different stages in the production process that invite errors in entrepreneurial judgment leading to overproduction. "There is overproduction, stoppage, and shutdown, reaction in turn on the making of plant and materials, cessation in the industries which will produce these, and general depression. The recurrence of commercial crises in this way is to be ascribed in the main to overproduction."[3]

More than 200 years ago Adam Smith viewed man's division of labor as the most beneficial factor of economic improvement. In the very first sentence of *The Wealth of Nations* Smith rejoiced about the division of labor. "The greatest improvement in the productive powers of labour, and the greater part of the skill, dexterity, and judgment with which it is anywhere directed, or applied, seem to have been the effects of the division of labour." In contrast to Smith, many modern writers are alarmed about the complexities and difficulties of finance

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"The capitalistic mode of distribution allocates to every participant the market value of his contribution to production: the businessman his profit, the investor his interest, the manager his salary, and the worker his wage."

and management that spring from the division of labor. At a loss for an explanation of depression and unemployment, they point at the separation of work into many different component operations through specialization. But no one concludes that man should return to less specialization, which would mean lower labor productivity and lower wage rates.

If improvements in the division of labor actually caused depression and unemployment, the business cycle in the most productive countries, with the most advanced division of labor, would have to be most severe and painful. Feverish booms would be followed by deep depressions. Americans would be affected more severely than Mexicans and Bolivians. In reality, depressions and unemployment are worse by far in Mexico and Bolivia than in the U.S. This is because the follies of government intervention are generally greater in Mexico and Bolivia than in the U.S.

If improvements in the division of labor actually caused depressions, business cycles should have grown worse in recent decades that witnessed world-wide improvements in the division of labor. In reality, recent recessions were demonstrably milder than the Great Depression of the 1930s. Moreover, every improvement in technology, every new instrument of production, which are the fruits of the division of labor, should usher in a new depression and mass unemployment. Every improvement in American computer technology, for example, should breed another cycle. It is obvious that economic reality differs from such conjectures.

To point at "overproduction" as a cause of business cycles is to ignore the unlimited needs and wants of most individuals. While millions of people are starving and thousands are perishing from hunger and want, it is insensible to speak of overproduction. Of course, it is understandable that the socialistic world that is chronically lingering in poverty and despair likes to point at capitalistic countries and charge them with "overproduction."

The Capitalistic System

Many writers in search of an explanation of the business cycle limit their indictment to the capitalistic system that permits private ownership of the means of production. One group finds fault with capitalistic modes of income distribution; another group centers its attention on the capitalistic process of production.

The capitalistic mode of distribution allocates to every participant the market value of his contribution to production: the businessman his profit, the investor his interest, the manager his salary, and the worker his wage. Some earn high incomes because they make great

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contributions to the economic well-being of their fellowmen; others earn little because they contribute little. The critics generally prefer a more equal distribution of income and wealth which, in their belief, would assure economic stability and full employment.

Lord Lauderdale (1759-1839) first pointed to consumption as the decisive factor for the quantity of labor that can be employed. "Forced parsimony" reduces the funds allotted to consumption and employment of labor.[4] Similarly, Thomas Robert Malthus (1766-1834) warned against the over-accumulation of capital. A more equal distribution of wealth would alleviate economic stagnation and decline. He favored public works as a means of employment and relief for the working classes: ". . . to assist the working classes in a period like the present, it is desirable to employ them in unproductive labors, or at least in labor, the results of which do not come for sale into the market, such as roads and public works."[5]

The business cycle theory of Lauderdale and Malthus, faulting the manner in which income is distributed, evoked answers by Jean Baptiste Say, David Ricardo and John Stuart Mill. They developed the so-called *law of markets,* which in essence denies that business cycles spring from "over-accumulation" and the manner in which income is distributed. By the end of the nineteenth century they reigned supreme in the economic world, which caused the critics to shift from the side of distribution to the side of production. The material conditions in the modern capitalistic order, in particular the roundabout methods of production, now came under attack for causing the business cycle.

Karl Marx in the main echoed the Lauderdale-Malthus explanation, but the thrust of his argument was "exploitation" rather than accumulation and inequality of incomes. Business crises are periodic climaxes of the conflicts inherent in the capitalistic system. Conflicts arise from the accumulation of capital and the growing proportion of fixed capital, which causes a decline in the consuming power of workers. The capitalists "exploit" labor and apply their ill-gotten gains, which they call "savings," to increase production. In short, they destroy their own markets by reducing "wage capital," the consuming power of laborers. Depressions temporarily restore the equilibrium between production and consumption.

Marx managed to present yet another explanation for business crises based on the life cycle of business capital. Because capitalists invest in spurts and bursts for various periods of time, "business undergoes successive periods of depression, medium activity, precipitancy, crisis. . . . A crisis always forms a starting point of large new investments."[6] In short, businessmen not only exploit their workers but also invest erratically and capriciously, which adds instability to exploitation. Their notorious behavior inevitably causes depression and unemployment.

A century after Marx, his countless followers throughout the world continue to explain business cycles as characteristics of capitalism. Total consumption, they propound as revealed truth, lags behind total production because of labor exploitation, which is robbery. Wherever Marxians come to power they summarily abolish private property in the means of production. Wherever they lack political power they openly advocate its abolition.

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Throughout the free world the Marxian explanation contends against other explanations, the most popular of which is that of John Maynard Keynes (1883-1946). This British economist was to become the economic patriarch of the free world. The foundation of the Keynesian structure is the Malthusian concept of effective demand which Keynes defines as "the aggregate income (or proceeds) which the entrepreneurs expect to receive . . . from the amount of current employment which they decide to give."[7] Professor Keynes made consumption the primary element of his economic order. Consumption limits production, not the other way around as the Classical economists had seen it. The "propensity to consume" becomes a basic independent variable. It brings into existence both production and capital as factors of production. Consumption, along with investment, is the basis of "effective demand."

Conceived during the Great Depression and resting on the idea of secular stagnation, Keynes' theory is a scheme of escape from depression by way of a planned or managed economy and socialized demand. The Classical economists built on the assumption of harmony or similarity of interests. In the footsteps of Karl Marx, Professor Keynes built on disharmony and conflict. The interests of savers and investors do not match, which in turn clash with the interests of consumers. Private capitalists are apt to be greedy exploiters or inefficient bunglers, or both, and do not require the rich rewards they usually pocket. To restore and maintain more desirable economic conditions, Professor Keynes recommended central control by politicians and officials. He called upon the state for protection from foreign competition and internal regulation to assure "equitable distribution of wealth and income" and "full employment."

Keynesian doctrines came to exercise great effect upon government policies throughout the world. The doctrines were not new; there were no new elements in the system, and no new proposals of policy. But the combination of elements, policies, and terminology was new. J.M. Keynes rebuilt an old machine and made it look new. And yet, despite its new appearance it was akin to the appointments of eighteenth century Mercantilists and Physiocrats, and related to the thought which the Classical economists meant to expose and explode.

Thus, most contemporary writers point at one or several features of the capitalistic order as the disturbing factors that are said to upset the economic equilibrium and thus create the business cycle. While they engage in heated debates about the particular feature or features that presumably cause the evil, they leave no doubt that the private property order is ever breeding instability and unemployment. This is why they are demanding that government, the political apparatus of coercion, remedy the stated defects or abolish the system.

Government Intervention

Only a few members of the Austrian school, in particular Ludwig von Mises and other writers in his footsteps, have drawn the extraordinary conclusion that, in the final analysis, government, as the creator of the monetary order and the monopolist of legal-tender currency, is solely responsible for the cycle. These economists deplore all notions and doctrines that place politicians and government officials in charge of the people's money and cause them to print ever more for the sake of economic "growth"

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Unemployment office, Pittsburgh, Pennsylvania, 1938. ARTHUR ROTHSTEIN

and full employment. In the judgment of these economists, the people must be liberated from the money monopoly and all politicians be banned from monetary matters.

In his explanation of the business cycle Professor von Mises combined given knowledge with new insights. He built on the Ricardian analysis of the effects of currency and credit expansion, on Böhm-Bawerk's theory of capital and interest, and on Wicksell's explanation of the potential gap between the "natural" rate of interest and the hampered market rate. Mises concluded that central banks tend to orchestrate processes of money and credit expansion that falsify interest rates. They create and emit new funds which lower interest rates and thereby entice businessmen to embark upon expansion and modernization. A feverish boom is created; wages and other business costs tend to rise.[8]

Drawing on the monetary theory of Mises, his teacher, Friedrich A. Hayek developed a theory that explains how monetary disruption al-

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ters relative prices by falsifying interest rates and the pattern of investment. The creation of money and credit generates a new source of demand of goods and resources to which business will react. At first, it generates a shift of spending in favor of future rather than current consumption. That is, it kindles an "investment boom" with rising employment by attracting resources that otherwise would have been consumed. The resources will remain so employed as long as the creation of money continues. It must be continued at accelerating rates in order to maintain the boom employment. If it is discontinued for fear of run-away price inflation, a readjustment commences in the form of depression. If, on the other hand, the monetary expansion continues at accelerating rates, it must ultimately lead to the breakdown of order and production, to disintegration of the division of labor and mass unemployment. A government that, for any reason, embarks upon such policies, holds a tiger by the tail that in the end will devour its keeper.[9]

The Austrian View

Austrian economists see eye to eye about the cyclical movements of economic activity. They agree that employment moves strongly with the basic changes in activity but typically is slower than other features of the cycle. In reaction to declining interest rates, activities preparatory to investment expenditure lead the way—such as incorporations, corporate appropriations for capital expenditures, issuance of building permits, contracts for construction, orders for machinery and equipment, rising commercial debt, and new equity issues. Employment together with general output and consumer prices are slower to react to the new situation. The reason is obvious: it is less onerous and exacting financially to seek a building permit or secure a line of bank credit than to engage and train human labor. Moreover, the building permit may be allowed to expire, the bank credit may remain unused, the equipment order may be shelved, but human labor cannot, with good conscience, be readily hired and then dismissed.

Labor costs per unit of output tend to lag behind other cycle phenomena. Labor contracts usually extend over lengthy periods of time, which keep total labor costs relatively constant but impose great variations in unit costs depending on the level of output. During the early boom when unit costs fall, the demand for labor tends to rise and wage rates and fringe benefits follow suit. When, later in the cycle, business activity slows down and unit labor costs soar, it is rather difficult to reduce wage rates and fringe benefits. Labor contracts may impose long-term commitments; but even if they do not, it is more difficult psychologically and more troublesome to labor relations to reduce wage rates and moderate labor conditions than simply dismiss labor. It is simpler to dismiss a worker than to reduce his wage rate because he can readily understand and accept unemployment, without lasting damage to his self-esteem, being dismissed for reasons of "lack of work"; it is more difficult by far to accept wage reductions because of "rising unit costs." Unemployment due to "lack of work" obviously places the responsibility on some mysterious factors over which the unemployed worker has no influence. But to be unemployed for reasons of "excessive labor costs" allocates some responsibility not only to the monetary authorities generating the cycle but also to the

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"All depressions in American history have had their beginning in a boom that was bred by government intervention."

unemployed themselves who may have contributed to the boost in costs and then refuse to suffer wage and benefit reductions.

Fluctuations in the number of employed workers are larger in capital goods and commodity-producing industries than in the service trades. After all, the cyclical fluctuations originate in the capital-goods and commodity-producing industries that readily respond to the currency and credit expansion. Businessmen embark upon construction that exhilarates all industries catering to business, that is, tools and dies, computers, steel, copper, lumber, and the like. It also explains why these industries are the first to suffer the fevers and chills of the business cycle. Moreover, the decision to expand or modernize a business is always entrepreneurial; it rests on the perception of the future which is uncertain. Businessmen are quick to change their construction orders when their outlook changes.

Wage disbursements fluctuate within a wider range than salary payments. In business usage, salary refers to a fixed monthly rate of pay, wage to an hourly rate. It is difficult for psychological reasons to reduce any rate of pay when business conditions deteriorate and labor productivity declines. But when labor costs must be reduced because business survival is at stake, employers are likely to begin their layoffs with hourly labor. In most cases this is unskilled or semi-skilled labor and requires very little training. It can be replaced readily and recalled easily without much training expense. On the other hand, employers generally are reluctant to dismiss salaried personnel, which is skilled labor, requiring lengthy schooling, training or apprenticeship before it can be employed productively. Moreover, generous employment compensation paid to unskilled labor tends to immobilize it, keeping it at company gates and waiting to be recalled. Unemployment compensation for skilled or professional labor loses its paralyzing effects when it becomes insignificant relative to the income that can be earned elsewhere. Skilled labor is quick to move on in search of other employment as soon as it is laid off, which makes employers rather reluctant to release it even temporarily.

A Common Cause

This sketch of the nature of business cycles rests on the common cause of all cycles: the money and credit expansion. Government, or its monetary authorities, may conduct it willfully and purposely in order to pursue some other objective, such as full employment, economic redistribution, or its own power and growth. Or, government may monopolize the issue of legal tender money and impose an institutional setting that is bound to disrupt the economic order. American history discloses no cycle that did not spring from this common cause. All depressions had their beginning in a boom that was bred intentionally or inadvertently by government intervention. The political powers to be who brought forth the first depression of 1819 also begot the depressions of 1839-1843,

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1873-1879, 1895-1897, 1920-1921, 1929-1938, 1949-1950, 1953-1954, 1957-1958, 1960-1961, 1966-1968, 1973-1975, 1981-1983. The unemployment that accompanied these depressions must be charged to the same political powers.

Some business cycles were merely disruptions of domestic activity; others encompassed trade and commerce throughout the world. The depression of 1920-1921 attained international scope; the depression of the 1930s assumed catastrophic proportions around the globe. Under the influence of like beliefs and doctrines, governments the world over conducted similar policies that bore similar fruit. Moreover, international interdependence and division of labor cause business cycles to spread from country to country. In small countries, especially, foreign trade and commerce may comprise the lion's share of economic activity, and foreign conditions may have a decisive influence on domestic matters. Foreign exports and imports, world commodity prices and interest rates usually play a vital role in the process of cycle transmission.

In recent years business cycles have become global disruptions that emanate from the U.S. In 1971, under U.S. leadership, all governments summarily abolished the last vestiges of the gold standard and enthroned the U.S. dollar as world money. They made the U.S. government and its Federal Reserve System the central banker of the world. This banker obviously may expand or contract his accommodations, dispense or withhold his favors and thereby determine the liquidity or illiquidity of the world. He may kindle a world boom or squash it with deflation and depression; the world depends on his discretion and wisdom.

Automatic Stabilizers

The new monetary order seems to aggravate the severity of the business cycle. The 1981-1983 depression proved to be immeasurably more painful and potentially more destructive than the depression of 1973-1975, which in turn was the worst since the Great Depression. And yet, despite the visible recurrence of painful cycles and in spite of their growing severity, many American economists point with confidence to the "automatic stabilizers" that are said to alleviate the disruptions. They derive comfort and confidence from the vast expansion of government, the "stabilizing influence" of the income tax, the growth of unemployment insurance and programs of social security. As a result of these changes, personal income has lost its direct link with the fluctuations of production. In fact, when industrial production falls significantly, total output may decline very little, and the aggregate of personal income, especially after-tax income, may not decline at all because government collects much less in taxes from corporations and individuals, but spends much more on unemployment insurance and social security payments.[10]

Unfortunately, all these "instruments of stability" are merely contemporary manifestations of the sovereign power over money and the right of government to inflate and depreciate the money. If it were not for this power and the ever-active printing presses that seek to stimulate and energize the sagging "private sector," a deep depression would engulf economic production. The vast expansion of government does not impart economic stability; it imposes a crushing burden on economic life and serves to destabilize it. Boosts in social security taxes

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or unemployment insurance taxes do not stimulate economic life; they depress it and create ever more unemployment.

When government resorts to inflation in order to stimulate activity and alleviate unemployment, it makes matters worse. Inflation disarranges the production process, rearranges the distribution of labor among industries, and thereby makes more and more workers dependent on the *continuation,* often even on an *acceleration,* of the rate of inflation. When, in the end, the inflation ceases or slows down, labor must scramble to readjust and return to more productive employment as prescribed by consumer choices and orders. The readjustment process may be slow and painful, the unemployment severe and prolonged.

Many economists rejoice about the visible shift of employment from basic industries to service industries, which affords new hope for more stable conditions. Manufacturing, mining, construction, and transportation are the most volatile industries; service industries such as health care and education are said to be more stable. But such hopes, too, are built on the power of government to engage in currency and credit expansion in order to finance the steady employment in the service industries, several of which, after all, either are owned outright by government or heavily subsidized by government. The steady employment of many doctors and teachers squarely rests on the taxing power of government and the effectiveness of its printing presses. It will draw to a close as soon as government loses some of its power either through tax rebellion or hyperinflation, or both.

Old Hazards and New Hope

The old hazards of cyclical unemployment continue to loom on many labor markets. After more than fifty years of strenuous contracyclical effort at all levels of government and nearly forty years of a congressional mandate articulated as the Employment Act of 1946, the forces that create cyclical movements have not vanished. In fact, they are growing in strength especially in those industries that rely on government favors. While the forces of depression are gaining, many Americans continue to cling to the expectation that the federal government will intervene with vigorous monetary, fiscal, and regulatory actions in order to check any depression that develops. But events are beginning to shake this confidence in political wisdom; they are likely to weaken it further in the years to come.

There is new hope. To distrust party politics and government coercion in economic matters is the beginning of economic knowledge and wisdom. □

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Don't Sell America Short

We have much to accomplish and much to be proud of in America.

by Robert Awenius

Mr. Awenius is a retired attorney and free-lance writer in Tulsa, Oklahoma.

Too many persons take a dim view of the problems that America has faced and solved—and in a negative manner disparage America and its future. They say that the glorious days of our country are over and will not be repeated in the future. Some even contend that we are no longer the world's leader; that Russia has supplanted the United States as a world power. Some of these prognosticators even say that we are through as a nation.

To many foreign nations, America has seemed to be an implausibility—but an actuality, a reality. Our coins contain the motto: *e pluribus unum*, meaning one out of many. But it takes more than a phrase to give unity to 235 million Americans, composed of adolescents and adults, men and women, whites, yellows and blacks, city dwellers, farmers and ranchers, liberals and conservatives, protestants and catholics, Jews and gentiles, factory workers and shop owners, public employees and private employees, and retired persons and workers. A foreigner looking on this melting pot of mixed human elements would expect to hear jeremiads and witness untold trouble, rather than to see the harmony that arises in this nation. Instead of wrenching disharmony, the republic proceeds on a note of unity.

Three centuries ago—1651 to be exact—Thomas Hobbes in England wrote a book entitled *Leviathan,* advocating the doctrine of sovereignty, setting forth the theory that all men fear each other and hence must submit themselves to the supremacy of the state in all secular and religious matters. In Hobbes' time that meant the King. Hobbes would have had considerable trouble accepting the fact of the American experiment of self-government outlasting many kingdoms, dictatorships and assorted despots.

America has thrived in an arena of free enterprise, where the self-regulating free market economy maximizes the free choice of our citizens. Here private entrepreneurs are relatively free to start a business—any business they wish—without obtaining permission of an official; and they can set their own prices and locate in any place in the country. This is in contrast to the authoritarian practices in much of today's world where centralized planning is the motif. Such planning is much akin to the mercantilist regulations of European economies in the seventeenth century. In this country the invisible hand of the market place can better organize an economy than the command economies of autocratic nations.

Yes sir, under our form of limited government and free enterprise, America is in good hands. Don't sell America short. □

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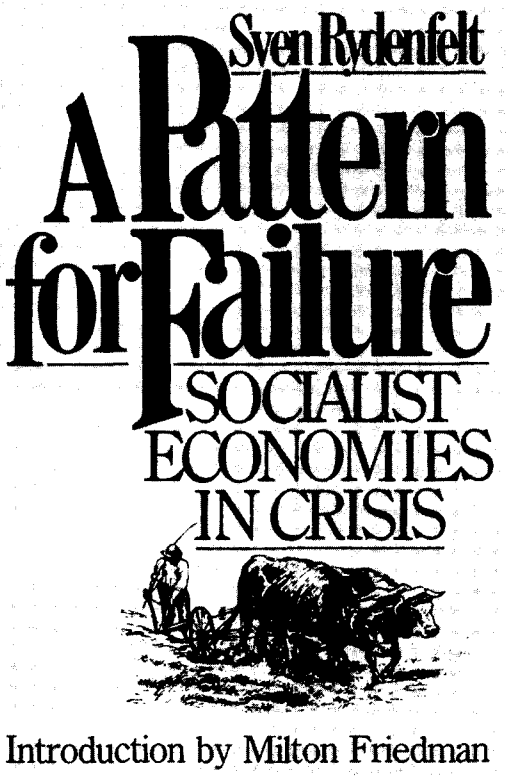

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Morality of the Market

by John Chamberlain

The Fraser Institute of Canada had a grand idea when it invited more than two dozen people of varying persuasions and expertise to talk about the morality of the market. The idea was to bring theologians together with economists of a predominantly secularist bias to discuss values as they may affect the ways of men and women who have their livings to make. The results of the Fraser symposium have been collected in a book called *Morality of the Market: Religious and Economic Perspectives*, edited by Walter Block, Geoffrey Brennan, and Kenneth Elzinga (The Fraser Institute, Vancouver, British Columbia, 601 pp.).

Frankly, the book has given me a bad time. I found it utterly fascinating in detail, but it is quite literally all over the place. The participants all had their say, with comments piled on comments, but, in the words of *The Rubaiyat of Omar Khayyam*, they come out as individuals by the same door that in they went.

Not that there is any basic disagreement between Milton Friedman on the one hand and the Reverend James M. Wall of the *Christian Century* magazine on the other about the role that fundamental religious convictions may play in economic affairs. Value assumptions cannot be avoided. The trouble comes from the inability of twenty-eight participants to reach any consensus about the will of God. The general assumption is that the Creator has endowed human beings with a moral sense, but does this mean that we must all be socialists in order to make human brotherhood a reality? The Catholic bishops come up with one set of answers when they say the decisions of the marketplace must be corrected if there is to be justice to the poor, but they may be missing the forest for the trees. So may certain spokesmen for Protestant Christianity, such as the contributors to the *Christian Century* that Edmund Opitz quotes in his paper about a magazine that he began to read in his school years.

J. Philip Wogaman, a professor of Christian Social Ethics, makes the point that a good economic system should allow for the concepts of stewardship, vocation and charity. He condemns laissez-faire economics for its alleged failure to protect the weaker members of the community and the common environmental inheritance of everybody. He likes the New Deal because it "worked" to bring about "beneficent" social change.

Wogaman is not quite a socialist, for he says there "may well be a need for private centers of economic power." But he is oblivious to the claims of the Vienna and Chicago economic schools that when government intervenes in the disposition of wealth there will be less money in the end available to care for the needs of growing populations. The paradox here is that welfare depends on capital earnings, but the earnings must fall

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short if the state takes more than a minimal percentage of the capital usufruct for its own purposes, whether beneficent or not. Wogaman is a clear thinker in his own realm, but it is fairly obvious that he has never seriously studied economics.

In his "overview" paper, John C. Bennett of the Union Theological Seminary explains his own evolution. He was originally influenced by the so-called Social Gospel, and by the Christian realism of Reinhold Niebuhr, which made him a Christian Socialist. But since 1950 he has, as he says, lost his dogmatism. Now he gives "weight" to "the pluralism and the incentives for efficiency and productivity" which are "characteristic" of capitalism. But in conceding that the market has its virtues Bennett has not really changed his mind. "One general conclusion that can be drawn," he says, "is that Christian teaching about finiteness and sin provide warnings against both a consistent socialism and a consistent faith in the market economy."

This sort of talk leaves me floundering. The Twentieth Century offers ample proof that socialism can't feed its own people. The private plots are what keep Russian peasants going. Collectivist agriculture in Africa has starved its millions. In Red China they are now turning to enterprise zones in an effort to restore the productivity that Maoism killed. Sweden's vaunted Middle Way struggles along by tolerating capitalist enterprise, but the boredom that comes with leveling incomes has resulted in a high suicide rate. Ludwig von Mises proved long ago that the problem of calculation is insoluble under complete socialism. Without a price system nobody would know how much wheat to plant, how much fertilizer to produce, or how many widgets to make.

In short, faith in a market system is a *sine qua non* if the human race is to endure and proliferate. Where people have lost their faith in the market, production has faltered, and the worst, as Hayek has said, have risen to the top to make slaves of the rest. It is an insult to God's intelligence to argue that Christian teaching about sin demands an equal amount of skepticism of both socialism and the free market. The latter lets more people live, which is in full accord with the Biblical injunction to increase and multiply.

Michael Novak's overview paper takes direct issue with Bennett's. Novak has no hesitation in saying that the market is far more concordant with the Christian vision of the human being than any system of production and distribution by political command. Voluntary exchange and autonomous choice, he says, are critical both for religious liberty and for freedom to preach the Word.

There is most certainly a lot to life besides economics. Edmund Opitz quotes Matthew Arnold on the instinct for intellect and knowledge, the instinct for beauty and poetry, the instinct for social life and manners, and the instinct for religion and morals. These demand expession just as much as the instinct for accumulation and expansion. But if there is no acumulation and expansion, there will be fewer people around to seek knowledge and beauty.

Ed Opitz, commenting on Ezra Mishan's paper, says there is a great deal of truth in Mishan's contention that economics and politics have usurped a position in our lives that their intrinsic merit does not deserve. But without science, technology and large-scale production four-and-a-half billion people would have little energy left to cultivate the non-economic values. The big question posed by this book is whether a market system or a command system is more compatible with finding scope for expressing the Arnoldian instincts. The answer should be the market system, but the babel of voices in this book is more confusing than clarifying. □

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Essays in the History of Liberty: Selected Writings of Lord Acton
edited by J. Rufus Fears

Liberty Classics, 7440 N. Shadeland, Indianapolis, IN 46250 • 558 pages, $15.00 cloth; $7.50 paperback

Reviewed by Tommy W. Rogers

Lord Acton (John Emerich Edward Dalberg-Acton), 1834–1902, was a major figure in the Liberal Catholic Movement, and was instrumental in transforming the writing of English history into a rigorously scientific discipline based on the model of German scholarship. The themes Acton expounded in his philosophic and journalistic activities as essayist, lecturer, and reviewer were those of individual liberty, political self-government, and unfettered scientific research.

The book opens with Acton's celebrated 1877 lectures on the history of freedom in antiquity and in Christianity. Acton argued that Christian civilization emphasized the dignity of the individual and offered him a gift of freedom beyond anything offered by Greece or Rome. He viewed the church as a force in society capable of limiting the power of the state; and "it is only by abridging the authority of states that the liberty of churches can be assured." By the same token, Acton condemned any effort by the church to wield secular power, as being the "absolute power which corrupts absolutely."

Here also are the essays on the Puritan Revolution and the rise of the Whigs. But of more interest to us are the essays on the colonies and on the American Revolution. A society emerged on these shores, Acton wrote, "more powerful, more prosperous, more intelligent, and more free than any other that the world has seen."

Acton analyzes the philosophic issues underlying the Civil War in America, declaring that "the one ruling element in the American war, which reduces all others to comparative insignificance, is the defense of the rights of self-government against the theory that there is a supreme, irresistible, and irresponsible power." Slavery, in his view, was not so much the cause of secession as the reason for the failure of secession and of the Confederacy. Acton felt that the Confederacy, apart from slavery, and viewing the Confederate Constitution as a political document, justified saying that "history can show no instance of so great an effort made by republicans to remedy the faults of that form of government (republican). Had they . . . called on Negroes to be partners with them . . . I believe that generous resolution would have conferred in all future ages incalculable blessing on the human race." In a letter to General Lee, Acton wrote: "I mourn for the stake which was lost at Richmond more deeply than I rejoice over that which was saved at Waterloo."

Acton's consistent rebel sympathies, which he extended to the Boers in South Africa, shaped his understanding of the issues at stake in the great struggle between Union and Confederation. Northern victory in the American Civil War, he argues, represented the triumph of political centralization over principles of federalism, self-government, and liberty under the law.

When Acton wrote that "Power tends to corrupt and absolute power corrupts absolutely," he spoke to generations past and future. How often has this phrase, this principle, been aptly descriptive of contemporary affairs! In an era when the state intrudes increasingly into the domain of the personal, the private and the spontaneous, Acton's insight into the meaning of human liberty and the dynamics which threaten its promise and exercise, remains salient and timely.

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Rivalry and Central Planning: The Socialist Calculation Debate Reconsidered
by Don Lavoie
Cambridge University Press, 32 E. 57th St., NY 10022 • 208 pages, $34.50

National Economic Planning: What is Left?
by Don Lavoie
Ballinger Publishing Co., Cambridge, MA 02138 • 291 pages, $25.00 cloth; Cato Institute, 224 Second Street, SE, Washington, D.C. 20003, $9.95 paper

Reviewed by Bettina Bien Greaves

Ever since the days of Karl Marx, opponents of the "establishment" have argued that socialism is the answer to all social ills. But Marx gave few clues as to the precise form that socialist society would take, and he attacked as "utopians" any who sought to describe it. Nevertheless, the inevitable inference to be drawn from his writings is that socialism would substitute central planning for the capitalist "anarchy of production" and for the isolated mercantilist interventions against which Adam Smith (1776) had directed his barbs.

After World War I, Marxian socialists gained control in several European nations. They set up commissions to study how to implement central planning, but they had no clear idea how to go about it and, except in Russia, the power of the central planners waned.

Into this controversy in 1920 ventured the late Ludwig von Mises, then a rising young economist in Vienna, Austria. Mises pointed out that if the factors of production were owned and controlled by a central planning authority there would be no markets for them. With no market for the factors of production, there would be no market prices for them. And without market prices, the planners would have no guideposts to help them decide what, when, where, how or how much to produce.

Mises' position that central planning couldn't be made to work with any degree of efficiency was largely ignored by the would-be planners. Thus Lenin tried to introduce Marxian planning in Russia in one fell swoop after the 1917 Communist Revolution. The attempt proved a disaster. The country was thrown into utter chaos. Lenin was forced to retreat and in 1921 introduced his New Economic Policy, which restored some function to the market. This Russian experience lent support to Mises' thesis that central planning couldn't be made to work.

In the 1930s, the economic calculation debate was revived. F. A. Hayek and the late Lord Lionel Robbins, especially, made important contributions, supporting, elaborating and helping to clarify Mises' reasoning. A number of Marxian socialists attempted to respond. Dr. Don Lavoie reviews the controversy anew in *Rivalry and Central Planning*, originally his doctoral dissertation

Lavoie begins with Marx's writings, extracting from them Marx's prescription for socialism, a painstaking process for it must be inferred from Marx's negative remarks about capitalism. Then Lavoie shows that all attempts to respond to Mises' 1920 challenge have failed to answer his critique of economic planning. Socialists over the years who have tried to answer Mises still do not realize that the central planning they advocate means state ownership and control of the factors of production, which precludes the development of market prices, disrupts the vital transmission of knowledge through the price system and, therefore, makes realistic economic calculation impossible. Mises' fundamental critique still stands.

* * *

The title of Lavoie's second book is *National Economic Planning: What is Left*?, a double entendre. In the first place, Lavoie asks, is anything to the ideological "left" of national eco-

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nomic planning? And secondly, he speculates, now that all serious attempts to introduce economic planning on a national scale have been abandoned, just what is left of them?

Lavoie begins by discussing three systems through which social activities may be coordinated—tradition, the market and planning. Tradition is admittedly suitable only as a means for coordinating activities in simple societies. The market, on the other hand, has led to the coordination of extensive and complex social activities. It has facilitated rapid experimentation and the development of countless new productive techniques. Impartial observers must admit that the extent of social cooperation and specialization under market coordination and the increase in production it has brought with it are remarkable. Lavoie then discusses the third possibility: economic planning. He concludes it has two fatal flaws.

The first flaw inherent in national planning is the totalitarian threat, the danger that a Hitler or a Stalin will gain control.

The second flaw is due to the knowledge problem, expertly developed by Lavoie in Chapter 3. How, Lavoie asks, will the central planners obtain the tremendous amount of widely dispersed information they need to coordinate successfully the complex activities of an entire economy, especially since much of this knowledge is unarticulated, existing only in the minds of scattered persons, in the form of ideas, plans or dreams?

The crux of Mises, and Lavoie's thesis, is that property should be privately owned and production planned by the private property owners. With free markets and competition among them, prices develop for goods, services and factors of production, indicating their relative value to consumers. For instance, as F. A. Hayek points out in "The Use of Knowledge in Society":

> Assume that somewhere in the world a new opportunity for the use of some raw material, say, tin, has arisen, or that one of the sources of supply of tin has been eliminated. It does not matter . . . which of these two causes has made tin more scarce [and thus more expensive]. . . . All that the users of tin need to know is that . . . they must economize tin.

Free and flexible market prices furnish private entrepreneurs with almost instantaneous knowledge about consumer wishes and also about the constantly changing supply of, and demand for, resources. When production is centrally planned, there are no market prices for the factors of production. Thus, national economic planning must inevitably founder for lack of the knowledge entrepreneurs obtain on the market from instant to instant through the medium of constantly fluctuating free competitive prices.

Lavoie's critique of *National Economic Planning* is masterful! It is also pertinent to the 1980s. Lavoie extends his analysis to many post-Marxian schemes, including such recent schemes as those of Wassily W. Leontief, Felix Rohatyn, Robert Reich and even Tom Hayden. Let's hope these recent planners read not only the few pages devoted to them but also earlier portions of the book where Lavoie demolishes the theory of planning.

* * *

I have two bones to pick with Lavoie. The first concerns his use of the labels "radical" and "reactionary." These words have no clear ideological meaning in themselves. A "radical" change in politics, according to Webster, is a sweeping or fundamental change in law or method of government. But the word itself does not specify the direction the change should take. Similarly, to advocate a policy of "reaction" gives no indication in

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itself as to what political or social condition one wishes to return to. Lavoie could have avoided confusion by using more descriptive terms such as "classical liberal" or "free trade internationalist" for "radical," and "interventionist," "statist," "militant nationalist" or "socialist" for "reactionary."

Secondly, I was most disappointed to find a scholar and economist of Lavoie's understanding and stature revealing such historical naivete as to attribute the *idea* of protectionist legislation to special groups of businessmen, bankers and industrialists. According to Lavoie, "the origins of planning in practice constituted nothing more nor less than governmentally sanctioned moves by leaders of the major industries to insulate themselves from risk and from the vicissitudes of market competition."

The responsibility for our present hodgepodge of interventionist programs that help some and hurt others must be laid at the door of well meaning if misguided voters and politicians, misled by mistaken intellectuals—"economists," professors, journalists and others—who believe that the remedy for almost any economic problem is a law. Businessmen, bankers and industrialists were not generally the culprits. Before the enactment of protectionist legislation, their interests are diverse; they are competitors. It is only *after* government grants them special favors that they acquire interests in common and form combinations to sponsor more legislation. To be sure, once protectionist legislation is in place many of them profit in the short run. Also many now seek continued government protection, privileges and benefits. This is not surprising, for once a program is established and businessmen have adjusted to it, they have a special interest in keeping that legislation in force. However, special interest groups are products of intervention, not vice versa.

* * *

Both these books make important contributions to economic understanding. It is Lavoie's hope that his *Rivalry and Central Planning*, which deals with the classical argument over economic calculation under socialism, will stimulate renewed discussion of this debate. *National Economic Planning*, which analyzes partial as well as total planning, should lead some modern-day advocates of government controls and regulations to question their own proposals. □

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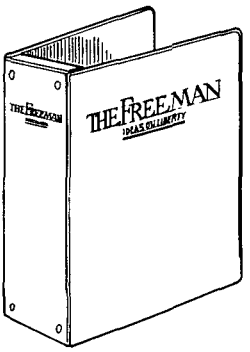

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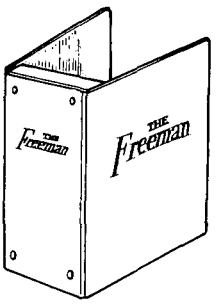

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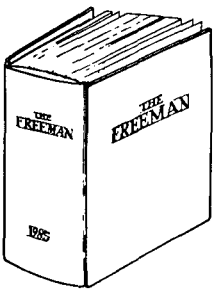

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